

Message Text

CONFIDENTIAL

PAGE 01 WARSAW 01061 01 OF 02 241651Z

46

ACTION EUR-12

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TO SECSTATE WASHDC 3523

CONFIDENTIAL SECTION 1 OF 2 WARSAW 1061

E.O. 11652: GDS

TAGS: EFIN, ECON, PL

SUBJECT: POLISH MULTIPLE EXCHANGE RATES COMPLICATE

PL-480 DEBT RESCHEDULING

REF: WARSAW 879

1. SUMMARY: THE FOLLOWING ANALYSIS OF POLAND'S JERRY-BUILT EXCHANGE-RATE SYSTEM SHOULD SHED SOME LIGHT ON THE POLISH GOVERNMENT'S ATTITUDE TOWARD THE ANNUITANTS ISSUE IN PL-480 DEBT-RESCHEDULING NEGOTIATIONS. ALTHOUGH POLAND'S OFFICIAL RATE OF EXCHANGE IS 19.92 ZLOTYS PER DOLAR (ZPD), ONLY ABOUT ONE PERCENT OF ITS FOREIGN-EXCHANGE TRANSACTIONS TAKES PLACE AT THAT RATE. A SOMEWHAT LARGER AMOUNT OF TRANSACTIONS OCCURS AT THE TOURIST RATE OF 33.32 ZPD, ALTHOUGH THESE TRANSACTIONS OFTEN HAVE NOTHING TO DO WITH TOURISM. MORE TRANSACTIONS OCCUR AT THE BLACK-MARKET RATE OF 80 TO 110 ZLOTYS PER DOLLAR THAN AT THE OFFICIAL AND TOURIST RATES COMBINED, AND MANY OF THESE TRANSACTIONS ARE NOT ILLEGAL. THE VAST BULK OF FOREIGN-EXCHANGE TRANSACTIONS (90 TO 95 PERCENT) OCCUR AT THE ROUGHLY 50-ZPD, CONFIDENTIAL, INTRA-GOVERNMENT RATE WHICH IS USED BY POLISH GOVERNMENT ENTITIES. THIS INTRA-GOVERNMENT RATE WOULD SEEM TO BE THE ONE THE POLISH CONFIDENTIAL

CONFIDENTIAL

PAGE 02 WARSAW 01061 01 OF 02 241651Z

GOVERNMENT CURRENTLY BELIEVES TO BE THE EQUILIBRIUM RATE

OF EXCHANGE. PRIVATE POLES AND SOME GOVERNMENT AGENCIES, HOWEVER, ARE WILLING TO PAY ABOUT TWICE AS MUCH FOR DOLLARS, AND THERE ARE SIGNS THE INTRA-GOVERNMENT RATE MAY BE INCREASED AS WELL. THE POLISH GOVERNMENT SEEKS TO REALIZE THAT U.S. ANNUITANTS COULD GET MORE ZLOTYS FOR THEIR DOLLARS IF THEY RECEIVED FREELY CONVERTIBLE DOLLAR INSTRUMENTS RATHER THAN THE RESTRICTED-CIRCULATION CHECKS THEY NOW RECEIVE. END SUMMARY.

2. POLAND'S OFFICIAL RATE OF 19.92 ZPD NOW SERVES PRINCIPALLY AS A BASE FROM WHICH THE HIGHER, MORE-FREQUENTLY-US ED RATES ARE CALCULATED, AND AS A DEVICE FOR EXTRACTING MORE FOREIGN EXCHANGE FROM "CAPTIVE" FOREIGN INDIVIDUALS AND COMPANIES UNWILLING OR UNABLE TO USE ONE OF THE MORE FAVORABLE RATES. ONLY ABOUT ONE PERCENT OF FOREIGN-EXHCNAGE TRANSACTIONS TAKES PLACE AT THE OFFICIAL RATE.

3. THE SO-CALLED TOURIST RATE OF 33.32 ZPD IS CALUCLATED AS THE OFFICIAL RATE PLUS A 66.7 PERCENT PREMIUM. THIS RATE THEORETICALLY IS AVAILABLE ONLY TO NON-RESIDENT FOREIGNERS, BUT MANY FOREIGNERS LIVING IN POLAND USE THIS RATE RATHER THAN SETTLE FOR THE 19.92-ZPD RATE OR RUN THE LARGER RISKS OF OPERATING ON THE BLACK MARKET. POLES WISHING TO BUY DOLLARS FOR TRAVEL ABROAD ARE ALLOTTED ONLY \$130 EVERY THREE YEARS, FOR WHICH THEY MUST PAY THE OFFICIAL RATE PLUS A 150-PRECENT COMMISSION, OR ABOUT 50 ZPD. ADDITIONAL DOLLAR REQUIREMENTS OF THESE POLISH TOURISTS MUST BE SECURED AT THE BLACK- MARKET RATE OF AROUND 100 ZPD. THE RAPIDLY GROWING NUMBER OF FOREIGN VISITORS FROM HARD- CURRENCY COUNTRIES NOW WELL OVER 500,000 A YEAR, ARE INCREASINGLY RELUCTANT TO SURRENDER MAY DOLLARS AT THE 33.32-ZPD RATE AND EITHER BRING ZLOTYS FROM ABROAD, WHERE THEY ARE AVAILABLE AT RATES RANGING FROM 60 TO 80 ZPD, OR DEAL WITH THE LARGE NUMBER OF BLACK-MARKET OPERATIVES, WHO OPENLY OFFER THE 100-ZPD RATE TO FOREIGN-LOOKING INDIVIDUALS IN AND AROUND THE TOURIST HOTELS. AT THE 33.32-ZPD RATE, TOURISM IN POLAND IS NO BARGAIN. AT THE RATE, POLAND IS ABOUT AS EXPENSIVE AS THE CHOICE TOURIST LOCATIONS OF WESTERN EUROPE AND THE QUALITY OF SERVICE

CONFIDENTIAL

CONFIDENTIAL

PAGE 03 WARSAW 01061 01 OF 02 241651Z

AND FACILITIES HERE IS MUCH BELOW WESTERN STANDARDS.

4. THE BLACK-MARKET RATE OF AROUND 100 ZPD IS AVAILABLE FOR MANY PERFECTLY LEGAL TRANSACTIONS. LOCAL PRODUCTS SOLD IN BOTH REGUALR STORES AND DOLLAR SHOPS ARE OFTEN PRICED TO REFLECT AN EXCHANGE RATE OF ABOUT 100 ZPD FOR THOSE WHO PAY IN HARD CURRENCIES. THE POLISH FIAT 125 P (1500CC), FOR EXAMPLE, COSTS

182,700 ZLOTY OR 1,740 DOLLARS, AN EFFECTIVE EXCHANGE RATE OF NEARLY 110 APD. IT IS ALSO MORE READILY AVAILABLE TO HARD-CURRENCY PURCHASERS.

5. THE BLACK MARKET IN FOREIGN EXCHANGE FLOURISHES SO OPENLY IN POLAND THAT ITS EXISTENCE MUST BE AT LEAST TACITLY APPROVED BY POLISH AUTHORITIES. IN A DEC. 22, 1974, INTERVIEW PUBLISHED IN "ZYCIE GOSPODARCZE", VICE-MINISTER OF FINANCE KRZAK OPENLY REFERRED TO THE BLACK MARKET, NOTING THAT IT HAD ONCE OPERATED AT A RATE AS HIGH AS 130 ZPD, BUT HAD DROPPED. THE RECENTLY-IMPOSED RESTRICTIONS ON DOLLAR AVAILABILITY FOR FOREIGN TRAVEL ARE SO SEVERE THAT THE GOVERNMENT MUST ASSUME ITS CITIZENS WOULD UTILIZE THE BLACK MARKET TO COVER MOST OF THEIR EXPENSES ABROAD. OTHER WISE THE LIMIT OF \$130 EVERY THREE YEARS WOULD HAVE AMOUNTED TO A VIRTUAL PROHIBITION OF FOREIGN TRAVEL, WHICH WOULD HAVE A VERY NEGATIVE POLITICAL IMPACT.

6 EVEN THOUGH THE EMBASSY HAS LONG ASSUMED THAT POLISH GOVERNMENT AGENCIES USED AN EXCHANGE RATE MUCH HIGHER THAN THE OFFICIAL 19.92 RATE FOR THEIR INTERNAL CALCULATIONS, WE ONLY RECENTLY SECURED AN OFFICIAL LISTING OF FOREIGN-EXCHANGE RATES USED BY POLISH GOVERNMENT AGENCIES ON AND AFTER MAY 3, 1974, WHICH SHOWED THAT A RATE OF 49.8 ZPD WAS AUTHORIZED FOR TRANSACTIONS WITH CONVERTIBLE-CURRENCY COUNTRIES. THESE AGENCIES HANDLE ALL OF POLAND'S IMPORT AND EXPORT ACTIVITY AND ALMOST ALL OF ITS SERVICE AND CAPITAL TRANSACTIONS AS WELL. THEY HAVE TO HAVE SOME WAY OF TRANSLATING THEIR FOREIGN-EXCHANGE TRANSACTIONS INTO ZLOTYS, IN WHICH THEY CONDUCT THE BULK OF THEIR OPERATIONS. ABOUT 90 TO

CONFIDENTIAL

CONFIDENTIAL

PAGE 04 WARSAW 01061 01 OF 02 241651Z

95 PERCENT OF POLAND'S FOREIGN-EXCHANGE TRANSACTIONS TAKE PLACE AT THE 49.8 " APD RATE.

CONFIDENTIAL

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PAGE 01 WARSAW 01061 02 OF 02 241653Z

46

ACTION EUR-12

INFO OCT-01 ISO-00 AID-05 L-02 EB-07 ABF-01 SP-02 NSC-05

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CONFIDENTIAL SECTION 2 OF 2 WARSAW 1061

7. WE HAVE COME ACROSS EVIDENCE THAT IN THE FALL OF 1973 THE GOVERNMENT'S INTERNAL EXCHANGE RATE WAS ABOUT 40 ZPD, AND THAT IT WAS RAISED LATER, PROBABLY IN MAY, 1974, TO ITS PRESENT 49.8 LEVEL. SUCH A "DEVALUATION" WAS PRESUMABLY RESORTED TO BECAUSE THE COUNTRY'S TRADE BALANCE HAS BEEN HEAVILY IN DEFICIT SINCE TRADE WITH THE WEST BEGAN TO BE ENCOURAGED BY THE GIEREK REGIME AFTER IT CAME TO POWER IN LATE 1970. IMPORTS FROM THE DEVELOPED COUNTRIES OF THE WEST ROSE BY 50 PERCENT IN 1972, 73 PERCENT IN 1973, AND 60 PERCENT IN 1974. AFTER DECADES IN WHICH TRADE WITH THE WEST WAS KEPT REGOROUSLY IN BALANCE, 1972 SAW THE APPEARANCE OF A \$350- MILLION TRADE DEFICIT WITH THE DEVELOPED COUNTRIES OF THE WEST. IN 1973, THIS DEFICIT GREW TO \$1.3-BILLION AND FOR 1974 IT WAS OVER \$2.0-BILLION LITTLE OF THIS DEFICIT CAN BE BLAMED ON THE PETROLEUM CRISIS, SINCE POLAND GETS MOST OF ITS ENERGY FROM COAL AND IMPORTS ALMOST ALL OF ITS PETROLEUM PRODUCTS FROM THE SOVIETS. PART OF THIS TRADE DEFICIT WAS DUE TOP THE SHARP INCREASE IN SUPPLIER-CREDIT FINANCING WHICH WAS OBTAINED BY THE GIEREK REGIME TO SUPPORT ITS AGGRESSIVE PROGRAM OF ECONOMIC MODERNIZATION THROUGH IMPORTS OF TECHNOLOGY AND EQUIPMENT FROM THE WEST.

ARMED WITH GOVERNMENT APPROVAL FOR LARGE-SCALE

CONFIDENTIAL

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PAGE 02 WARSAW 01061 02 OF 02 241653Z

PURCHASES FROM WESTERN COUNTRIES, POLISH ENTERPRISES HAVE BEEN BUYING HEAVILY, CAPITALIZING ON AN INTRA-GOVERNMENT EXCHANGE RATE WHICH APPARENTLY OVER-VALUED THE ZLOTY.

8. POLAND'S TRADE WITH ITS CEMA PARTNERS HAS REMAINED QUITE EVENLY BALANCED AND HAS NOT GROWN NEARLY AS

QUICKLY. BECAUSE OF THIS "OPENING TO THE WEST", THE SHARE OF POLAND'S IMPORTS WHICH CAM FROM THE DEVELOPED COUNTRIES OF THE WEST INCREASED FROM 25 PER-CENT IN 1970 TO ABOUT 55 PERCENT IN 1974. IN ABOUT MAY OF 1974, POLISH AUTHORITIES APPARENTLY DECIDED THEY HAD TO TAKE MEASURES TO CURB THIS FLOOD OF IMPORTS FROM THE WEST. CONSEQUENTLY, THE "DEVALUED" THE INTRA-GOVERNMENT ZLOTY BY ABOUT 25 PERCENT FROM 40 ZPD TO 49.8 ZPD. JUDGING BY THE CONTINUED LARGE TRADE DEFICITS EXPERIENCED DURING THE LAST MONTHS OF 1974 AND THE RECENT PUBLIC COMMENTS BY GOVERNMENT OFFICIALS THAT FURTHER STEPS WILL HAVE TO BE TAKEN TO CURB IMPORTS, THE MAY "DEVALUATION" PROBABLY WAS NOT ENOUGH. ALTHOUGH POLAND CLAIMS TO HAVE EXCAPED THE IMPACT OF WESTERN INFLATION, OFFICIAL STATISTICS SHOW THE COST OF LIVING ROSE 5.7 PERCENT LAST YEAR. CONTACTS IN THE MINISTRY OF FOREIGN TRADE HAVE TOLD US FURTHER PRICE INCREASES SHOULD BE EXPECTED ON ITEMS OTHER THAN THOSE "BASIC" GOODS WHOSE COST TO THE CONSUMER HAS BEEN FROZEN BY THE GOVERNMENT. THE NEW AVERAGEING SCHEME FOR SETTING CEMA INTERNAL PRICES (REFTEL), PARTICULARLY THE SHARP INCREASE IT IS EXPECTED TO BRING IN THE COST OF PETROLEUM, WILL ADD A NEW SOURCE OF UPWARD PRESSURE ON THE POLISH COST OF LIVING.

9. IF THE POLISH GOVERNMENT CONTINUES TO LIBERALIZE ITS ECONOMY AND INCREASE ITS ECONOMIC INVOLVEMENT WITH THE WEST, AS IT SHOWS EVERY INTENTION OF DOING, IT WILL HAVE TO REACH SOME MORE SATISFACTORY SOLUTION TO ITS EXCHANGE-RATE PROBLEM. AT A MINIMUM, IT WOULD SEEM THAT THE INTRA-GOVERNMENT EXCHANGE RATE WILL HAVE TO BE "DEVALUED" FURTHER FROM ITS CURRENT 49.8-ZPD LEVEL.

CONFIDENTIAL

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PAGE 03 WARSAW 01061 02 OF 02 241653Z

10. COMMENT: IN THIS COMPLICATED WORLD OF POLISH EXCHANGE RATES, THE U.S. ANNUITANTS FIND THEMSELVES IN A STRANGE POSITION. A POLISH GOVERNMENT WHICH VALUES THE DOLLAR AT ALMOST 50 ZLOTYS FOR ITS OWN PURPOSES AND FINDS THAT IT PROBABLY SHOULD VALUE IT HIGHER, LEGALLY CAN OFFER THE RESIDENT ANNUITANTS ONLY 19.92 ZPD FOR THEIR ANNUITANT CHECKS. IF THESE ANNUITANTS RECEIVED REGULAR, FREELY-CONVERTIBLE DOLLAR INSTRUMENTS RATHER THAN THE RESTRICTED-CIRCULATION CHECKS THEY NOW RECEIVE, MANY OF THEM PROBABLY WOULD NOT SETTLE FOR THE 60-ZPD RATE, BASED ON PL-480 ZLOTYS, EVEN IF WE CONTINUED TO MAKE IT AVAILABLE. RATHER, THEY WOULD RUN THE RISK OF EXCHANGING THEIR DOLLARS FOR THE MUCH MORE ATTRACTIVE

RATES AVAILABLE ABROAD OR IN THE LOCAL BLACK MARKET.
POLISH AUTHORITIES ARE AWARE OF THIS AND THIS AWARENESS
MUST BE FACTORED INTO THEIR APPROACH TO THE ANNUITANTS
ISSUE IN THE PL-480 DEBT-RESCHEDULING NEGOTIATIONS.
DAVIES

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